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IN THE

Supreme Court of the United States

OCTOBER TERM, 1937

No. 33

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

v.

RAYMOND I. BASHFORD.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF FOR THE RESPONDENT.

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OPINIONS BELOW.

The opinion of the United States Board of Tax Appeals (R. 127-143) is reported in 33 B. T. A. 10. The opinion of the Circuit Court of Appeals (R. 202-206) is reported in 87 Fed. (2d) 827.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered January 22, 1937 (R. 206). The petition for writ of certiorari was filed April 22, 1937, and was granted May 24, 1937 (R. 208). The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED.

Taxpayer, an individual, owned stock in Corporation A (Peerless). Corporation C (Atlas) desired to obtain control of the business and assets of A and of its wholly owned subsidiary (Black Diamond), and of another corporation, B (Union), all four corporations being engaged in the same line of business. Pursuant to agreements between C on the one part and owners of substantially all of the stock of A (including taxpayer) and of B on the other part, a plan of reorganization, conceived by C, was consummated. In accordance with said agreements C acquired from the stockholders of A and B substantially all of the stock of these corporations in exchange for a substantial amount of its own stock, cash and approximately 43 per cent of the common stock of a new corporation, D (Peerless-Union), which C organized pursuant to the plan. C, as a part of the plan, delivered to D, the stock of A and B which, after a transfer of all their assets to D, were dissolved. Through consummation of and as a part of the plan from its inception, C acquired all the preferred stock and approximately 57 per cent of the common stock of D, the same being the only classes of D's stock.

Petitioner has conceded that the consummation of the plan resulted in a statutory reorganization to which D was a party and hence that the gain, if any, to taxpayer realized through his acquisition of the stock of D is non-taxable. Taxpayer paid the tax upon the gain realized through his acquisition of cash. The sole remaining question is whether the

gain resulting from the acquisition by taxpayer of stock in C is taxable. This depends upon whether the stock of C is stock of a corporation, "a party to the reorganization" under Section 112 (b) (3), or "other property" under Section 112 (c) (1) of the Revenue Act of 1928.

STATUTE AND REGULATIONS INVOLVED.

The statute and regulations involved will be found in the Appendix, *infra*, pp. 37-40.

STATEMENT.

The facts in this case, except those disclosed by the uncontradicted testimony of two witnesses, were stipulated before the Board of Tax Appeals (R. 19-37). Attached to and made a part of the stipulation as exhibits (R. 37-126) are the several documents and agreements referred to herein. Separate findings of fact were not made by the Board. Its findings of fact were included in its Opinion (R. 127-143) and may be summarized as follows:

Prior to October 7, 1930, Peerless Explosives Company, Black Diamond Powder Company, its wholly owned subsidiary, and Union Explosives Company were corporations engaged in the manufacture and sale of explosives, as was Atlas Powder Company. Peerless and Union were not only competitors of Atlas but also substantial customers of that Company since they purchased from it large quantities of chemicals used in the manufacture of their products. (R. 128-129)

The President of Atlas, not satisfied with its relationship with Peerless and Union, conceived the plan of acquiring control of the business of these companies by means of reorganizing them into a new corporation to be controlled by Atlas (R. 129).

In order that the plan might not be blocked prematurely by competitive interests and to assure reasonable terms not otherwise obtainable (R. 129, 186) Atlas acted through in-

dividual agents, Seligman and Fletcher, both being experienced in the powder business through former connection with Atlas and both being personally acquainted with many of the stockholders of Peerless and Union (R. 129-130). Atlas instructed its agents that it did not desire to purchase either the assets or stock of Peerless or Union but to reorganize them by exchanges of stock into a new company which would be controlled by Atlas (R. 130).

For the same reasons that it acted through agents, Atlas did not disclose its identity at the inception of the negotiations (R. 129, 186). During the preliminary negotiations with the majority stockholders, however, Atlas' agents let it be known that they represented a strong financial interest which would finance the reorganization and that the principal stockholders of Peerless and Union would become stockholders and officers of the new company (R. 130). The identity of Atlas was disclosed in July, 1930 (R. 186, 195) when the majority stockholders of Peerless and Union gave their oral assurance that they would exchange their stock on the basis of a plan substantially similar to that consummated under the written contracts entered into on October 7, 1930 (R. 130).

The main features of the reorganization plan were that Peerless (with Black Diamond) and Union were to be consolidated into a new company, Peerless-Union Explosives Company; that the stockholders of the old companies would receive for their stock, cash, Atlas stock and stock of the new company. Atlas in exchange for the preferred stock and a majority of the common stock of the new company, on its part, was to furnish the new company with working capital and with sufficient cash and shares of its own common and preferred stock to complete the exchanges with the stockholders of the old companies. (R. 130-131)

As a preliminary step, Atlas caused the incorporation of the new company on September 22, 1930, for the purpose of acquiring the business and assets of Peerless, Black Diamond and Union, and subscribed for and was issued all of

its original authorized capital stock, the same being 10 shares of common and 10 shares of preferred. Subsequently, on October 6, 1930, the authorized capital stock of the new company was increased to 100,000 shares of common stock of no par value and 50,000 shares of preferred stock of $100 par value. (R. 131)

On October 2, 1930, the Board of Directors of Atlas approved the proposed reorganization and the incorporation of the new company and authorized and directed its officers to invest in the capital stock of the new company up to an aggregate of 21,732 shares of its preferred stock and 32,198 shares of its common stock, and in consideration therefor to deliver to the new company $960,560.25 in cash, 6318 shares of Atlas preferred stock on the basis of $100 per share, and 8,712½ shares of Atlas common stock on a basis of $66.66-2/3 per share (R. 131-132). At the same time Atlas authorized and empowered its transfer agent to make such original issue of the shares of its stock as, with available treasury stock to be devoted to the purpose, would enable Atlas to fulfill its obligations under the plan in connection with the transfer of its stock (R. 43). Atlas' investment, as authorized, was consummated on or about October 7, 1930 (R. 136).

On October 7, 1930, the Respondent taxpayer, one of the majority stockholders of Peerless, and the other majority stockholders of Peerless and of Union, entered into written contracts with the agents of Atlas to deliver their shares of stock in their respective corporations to said agents in exchange for cash, shares of common stock in the new company and common and preferred shares of stock in Atlas in amounts agreed on in the plan (R. 132-134). The contracts provided a basis of exchange with the minority stockholders (R. 133, 134-135), and also certain warranties as to the employment of said majority stockholders by the new company, as to the acquisition by the new company of the assets of the old companies and the assumption of their liabilities, and their dissolution (R. 133-135).

On the same day the agents of Atlas and the new company entered into a written contract wherein the agents agreed to exchange the stock of Peerless and Union, to which they were entitled under their contracts with the stockholders of those corporations, for cash, stock of Atlas and stock of the new company in the amounts required by the agents to consummate the exchanges under their contracts with the said stockholders (R. 135). In addition Atlas agreed, in individual agreements with said majority stockholders, to reimburse them for any income tax resulting from the recognition of gain derived either from the receipt of Atlas stock therein or upon the subsequent sale of said stock (R. 135). Prior to October 7, 1930, the agents of Atlas had secured options on practically all of the minority stockholdings in Peerless and Union (R. 135-136).

On October 7, 1930, all of the transfers and exchanges provided for in the above-mentioned agreements and the plan of reorganization were made. As a result of the consummation of the agreement between the agents of Atlas and the new company, the latter became the owner of practically all of the stock of Peerless and Union. The old companies then transferred their assets to the new company and were dissolved (R. 136).

Upon completion of the stock exchanges on October 7, 1930, the shareholdings in the new company were as follows (R. 136):

	Shares	Shares	Percentage of total
Preferred stock	21,732	.....	
Owned by Atlas.....	.....	21,732	100%
Common stock	64,252.54	.....	
Owned by Atlas.....	.....	37,198	57% plus
Owned by former stockholders of Peerless and Union.....	27,054.54	.....	43% minus

The taxpayer, one of the majority stockholders of Peerless, received in exchange for 2534.38 shares of the common

stock of that company, the following: $25,306.67 in cash; 625 shares of the preferred and 1344 shares of the common stock of Atlas, and 2720.08 shares of the common stock of the new company (R. 138). Taxpayer included all of the cash received as taxable income in his return for the year 1930 claiming no cost or other basis for his stock in Peerless (Ex. "R").

The Commissioner asserted a deficiency against the taxpayer upon the theory that there had been a statutory reorganization effected between the three old companies and the new company but that Atlas was not a party to such reorganization and that, therefore, its stock received by the taxpayer in the exchange should be treated as "other property" and the gain thereon recognized along with the cash received under the provisions of Section 112 (c) (1) of the Revenue Act of 1928 (R. 12-13).

Before the Board, the Commissioner changed his position and claimed that no statutory reorganization was effected, but that the entire transaction constituted a sale (R. 139).

The Board of Tax Appeals rejected the contentions of the Commissioner and held that a statutory reorganization had been effected between the three old companies and the new company and that Atlas was a party thereto by reason of the fact that it had acquired all of the preferred stock and a majority of the common stock of the new company in a transaction in which, without the participation of Atlas, there would have been no reorganization (R. 141). The Board also found that Atlas was the mainspring of the entire proceeding and hence that the facts in that respect were quite similar to those in *Fifth Avenue Bank of N. Y., Executor*, v. *Commissioner*, 31 B. T. A. 945 (Aff'd. by the Circuit Court of Appeals for the Third Circuit, 84 Fed. (2d) 787). Moreover it found the facts in the instant case to be even stronger for the taxpayer in that Atlas acquired a majority of all classes of stock of the new company which "unquestionably made it a party to the reorganization"

(R. 142) within the literal terms of Section 112 (i) (2) of the Revenue Act of 1928.*

In the court below the Commissioner reverted to the original position (R. 11-14) taken by him in asserting a deficiency, to-wit: that while there was a reorganization effected through a consolidation of the old companies into the new, Atlas was not a party thereto (Petitioners brief below, 8).

The Court, however, held that Atlas was a party to the reorganization within the literal terms of the statutory definition because Atlas had acquired a majority of the stock of all classes of the new company in connection with the consolidation of the three old companies under the plan of reorganization (R. 205). It also held that even if Atlas had not thus come within the literal terms of the statutory definition, it was a party to the reorganization transaction, as that language is commonly understood, because of its intimate connection with the reorganization of the other corporations (R. 205-206).

SUMMARY OF ARGUMENT.

The exchanges and transfers herein constitute one transaction under a plan of reorganization pursuant to corporate business.

The foundation of the plan, from its inception, was in substance the agreements between Atlas and the stockholders of Peerless and Union which contemplated that Atlas, upon acquisition of substantially all of the stock of those companies through exchanges, would transfer the stock thus acquired to the new company which it would control, and would cause the assets and business of the old companies to be transferred to the new company. The plan provided for

*This point was apparently overlooked by the Petitioner in the "Statement" of facts in his Brief (pp. 7, 8), in which it is indicated that the decision of the Board was based solely upon its former decision in *Fifth Avenue Bank of N. Y., Exr.* v. *Commissioner, supra.*

a continuance of interest on the part of the "stockholders"* in the business formerly conducted by Peerless and Union by insuring their acquisition of a substantial stock interest in both the new company and Atlas.

Petitioner concedes that Atlas did acquire a majority of the stock of the new company (Pet. Br. 6) and that the old corporations were consolidated into the new company, resulting in a statutory reorganization in which the new company was "a party" in the statutory sense (Pet. Br. 9). The sole issue here is whether Atlas was also a party to that reorganization. In presenting its argument on this point, respondent contends:

(I) That Atlas was "a party to a reorganization" because it comes within the literal terms of Section 112 (i) (2) of the Revenue Act of 1928;

(II) That Atlas was "a party to the reorganization" within the terms of Section 112 (b) (3) because of its indispensable participation in and inseparable connection with the entire transaction.

It will be observed that the Court below found that to sustain its decision it was sufficient to determine that Atlas was a party to the reorganization on only one of the above grounds, but it concluded that Atlas was a party thereto upon both grounds.

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*The majority stockholders of Peerless and Union are herein referred to as "stockholders."

ARGUMENT.

I.

Atlas was "a party to a reorganization" because it comes within the literal terms of Section 112 (i) (2) of the Revenue Act of 1928.

1. All of the exchanges and transfers here involved constitute but a single transaction under a plan of reorganization pursuant to corporate business, in each step of which Atlas actively participated *and as the result of which it acquired, pursuant to the plan from its inception, a majority of the stock of all classes of the new company and therewith control of the assets and business of Peerless, Black Diamond and Union.* (R. 139, 141)

In asking this Court to reach a contrary conclusion on the above stated issue, Petitioner bases his argument on the premise that Atlas did not participate in the reorganization of Peerless* as defined in Section 112 (i)(1)(A)(Pet. Br. 10); that Atlas' participation in the reorganization was limited to the participation of its subsidiary and cannot, therefore, reasonably be said to have been a party to it under Section 112 (i)(2) (Pet. Br. 10, 13). Whether that premise can be established in fact can best be determined by an analysis of the findings of the Board of Tax Appeals.

In consummating this transaction, all of the transfers and exchanges were made as provided for in the agreements of October 7, 1930, between the parties (R. 136). The principal agreements, all executed on October 7, 1930, were those of Atlas (either directly or through agents) on the one part, and "stockholders" on the other part, wherein the latter agreed to exchange their majority stockholdings in their respective companies for a substantial amount of Atlas stock, cash, and stock of the new company. These agreements made provision for exchanges with the minority

*For some reason Petitioner makes no mention of "Union" and "Black Diamond".

stockholders, substantially all of whose stock was acquired by Atlas under the plan. (R. 132-136, 141)

Under the above-mentioned agreements with the "stockholders" Atlas agreed to cause the three old companies to transfer their assets and business, including their liabilities to the new company formed by Atlas pursuant to the plan for the purpose of continuing the operation of the businesses thus consolidated under its control and to supply the new company with additional working capital of approximately $300,000 (R. 131-133).

To complete the exchanges and commitments made by Atlas in the aforementioned agreements with the majority and minority stockholders of Peerless and Union in which Atlas was obligated to deliver to said stockholders cash, common and preferred stock of Atlas and approximately 43 per cent of the stock of the new company, Atlas invested in the capital stock of the new company up to an aggregate of 21,732 shares of its preferred stock and 32,198 shares of its common stock, necessary to give it control, in consideration for 6,318 shares of Atlas preferred stock, 8712½ shares of Atlas common stock and $960,560.25 in cash (R. 22-23, 131-132). And at the same time Atlas, through its agents, entered into a contract with the new company (R. 83-88, 135) pursuant to which said agents transferred to the new company substantially all of the stock of the old companies in exchange for $632,150 in cash, shares of Atlas common and preferred stock previously acquired by the new company, as stated, and 32,054.54 shares of the common stock of the new company which cash and securities, except 5,000 shares of the common stock of the new company issued to Fletcher and Seligman as nominees of Atlas (R. 136-138), were delivered, pursuant to instructions of said agents, to the stockholders of Peerless and Union (R. 135-136). The new company retained in excess of $300,000 of the cash invested by Atlas for working capital (R. 133).

As the Court stated in *Watts* v. *Commissioner*, 75 Fed. (2d) 981, 982, "The plan of reorganization was the contract

made and performed". Since the agreements and transactions were found by the Board to represent the plan of reorganization as conceived and executed (R. 136, 139), it follows that Atlas acquired its stockholdings in the new company in the reorganization.

There is no basis for its characterization by the Petitioner as a circuitous and involved scheme. Fletcher and Seligman (found by the Board to be the agents of Atlas (R. 141)) in negotiating with the "stockholders" were instructed that they should consider no plan which did not provide for the consolidation of the old companies into a new one which Atlas would control (R. 130, 164). The "stockholders" insisted upon retaining a substantial interest in the assets and business transferred through a stock interest in Atlas and the new company and through being retained in the latter's employment (R. 131, 135, 175, 185). Atlas, on its part, realized from the beginning that the acquisition of the stock of Peerless and Union, except by exchanges substantially as effected, would not only require a prohibitive amount of cash but would not satisfy the "stockholders" (R. 175). Atlas considered it of vital importance to continue the business of the old companies through a separate corporation (which it would control) to prevent serious loss of customers and good will (R. 190-191). The Board found that said agents disclosed the identity of Atlas as soon as the "stockholders" gave "oral assurances they would exchange their stock in Peerless and Union substantially on the basis of the written contracts finally entered into * * *" (R. 130). This was in July, 1930 (R. 195, 205). The contracts between the agents of Atlas and the "stockholders" disclose on their face the identity of Atlas throughout (R. 53-55, 73-75). In the "Tax Guarantee Contracts" with the "stockholders", Atlas was a direct signatory. In these contracts it was provided that the "stockholders" would be reimbursed for either a tax resulting from their receipt of Atlas stock or its subsequent disposition (R. 88-92, 92-97, 97-101). The Court below sustained

this and all of the other administrative findings of the Board as based upon sufficient evidence and therefore conclusive upon it, citing in support, *Beech* v. *Commissioner*, 82 Fed. (2d) 42, and *Phillips* v. *Commissioner*, 283 U. S. 589 (R. 206).

While Petitioner admits that a statutory reorganization was effected in the consummation of the transaction, wherein Peerless, Union and Black Diamond were consolidated into the new company, he contends that Atlas was not a party "within the literal terms of the statutory definition nor within its purpose, * * * " (Pet. Br. 9), because "at no stage in the transactions in this case was Atlas a party to the Peerless reorganization; at the completion as at the outset of these transactions its only relation to the Peerless reorganization was that its subsidiary, the new company, was a party" (Pet. Br. 20), and even that " * * * Atlas was not a party to those exchanges between the old companies and and the new company which did constitute a statutory reorganization, and acquired neither the assets nor any of the stock of the old companies" (Pet. Br. 13).

Whatever might result from the application of the statute to such assumptions of fact need not concern us here for they are contrary to the specific and unchallenged findings of the Board, referred to before in this Argument. Fundamentally, the entire argument of Petitioner is based upon a misconception of what the plan was and how it was carried out. Petitioner's conclusions are necessarily erroneous because they are based on false premises.

In direct conflict with Petitioner's conclusion that Atlas' "* * * only relation to the Peerless reorganization was that its subsidiary, the new company, was a party", using that term in accordance with its ordinary meaning, the facts reveal that no argeements were entered into between the "stockholders" and the new company, except the "Tax Guarantee Contracts" above referred to, in which, as stated, Atlas was also a *direct* party, nor was the new com-

pany a party to any exchange or transfer with the "stockholders".

In fact, all the exchanges and transfers were consummated by Atlas either acting directly or through its agents. Even the actual transfer of the assets of the old companies to the new was effected by Atlas. Before the new company could acquire the assets it was first necessary for Atlas to transfer to it the stock of the old companies.

Thus the Board and the Court below held that the several transfers and exchanges constituted but *one* transaction, under one plan of reorganization both in their inception and execution, that in each step Atlas played a dominating and active part either through direct participation, by its agents, or through its controlling stock interest in the new company and that through completion of the exchanges aforementioned Atlas became the owner of approximately 57 per cent of the common stock and all of the preferred stock of the new company.

The Court below sustained the Board's summary of its findings that:

> "The main features of the plan were that Peerless, Union and Black Diamond were to be consolidated into a new company, Peerless-Union Explosives Corporation, that the stockholders of the old companies would receive for their stock in the old companies stock in the new company, stock in Atlas and some cash. Atlas on its part was to furnish the new company with sufficient cash and sufficient shares of its own common and preferred stock to complete the transaction. In return it was to receive sufficient common and preferred stock in the new company to assure its control." (R. 203.)
>
> * * * * * *
>
> "* * * Atlas was the mainspring of the entire proceeding and without its participation there would have been no reorganization and consolidation into the new company." (R. 205-206.)

2. The fact having been established that the several transfers and exchanges here were interdependent steps in and

component parts of one plan of reorganization, the Petitioner may not break up that single transaction into parts to assert a tax. *Prairie Oil and Gas Co.* v. *Motter*, 66 Fed. (2d) 309 (C. C. A. 10th); *Tulsa Tribune Co.* v. *Commissioner*, 58 Fed. (2d) 937 (C. C. A. 10th); *Howard* v. *Commissioner*, 56 Fed. (2d) 781 (C. C. A. 6th), certiorari denied, 287 U. S. 619; *Sage* v. *Commissioner*, 83 Fed. (2d) 221 (C. C. A. 2nd); and *Thurber* v. *Commissioner*, 84 Fed. (2d) 815 (C. C. A. 1st). The Courts have reached the same conclusion where the Commissioner has relied on the inseparability of the plan to prevent a taxpayer from avoiding a tax by breaking it into parts. *Bassick* v. *Commissioner*, 85 Fed. (2d) 8 (C. C. A. 2nd), certiorari denied, 299 U. S. 592; *Ahles Realty Corporation* v. *Commissioner*, 71 Fed. (2d) 150 (C. C. A. 2nd), certiorari denied, 293 U. S. 611; *Starr* v. *Commissioner*, 82 Fed. (2d) 964 (C. C. A. 4th), certiorari denied, 298 U. S. 680.

An analysis of the facts in the above cited cases reveals plans of reorganization, some of the steps of which were interdependent only in that they were provided for in a single plan of reorganization. They were related steps in the sense that one step might not have been consummated but for the *agreement* of the parties to consummate other steps, yet, unlike the present case, they were complete in that chronologically one could be completed without all of the steps being completed. Some of these cases, for instance, involve the exercise of options, the declaration of special dividends with exchange rights and the purchase by one party of stock received by another party in the reorganization. It is in this respect that the facts in the instant case are even stronger in support of the conclusion reached by the Courts in the cases above cited.

The Petitioner having erroneously assumed that the acquisition by Atlas of the stock of the new company was a step separate and apart from the reorganization which admittedly resulted here, erroneously concludes that it should be treated separately in its tax significance.

3. Even if the transaction as a whole, in the instant case, is to be broken up into parts or steps to determine their separate tax significance, it will be observed that viewed from the standpoint of the actual exchanges of stock and transfers, as contrasted with the Petitioner's arbitrary division of the transaction (Pet. Br. 10), each exchange viewed in the light of its ultimate completion constitutes a statutory reorganization. The first and most essential exchange was that made pursuant to the agreements between Atlas and the stockholders of the old companies wherein the latter exchanged substantially all of the stock of Peerless and Union for a substantial amount of stock of Atlas, cash and stock of the new company. This was a reorganization. *Helvering* v. *Watts*, 296 U. S. 387.

In the second corollary and subsidiary exchange made pursuant to the agreement between Atlas and the new company, the latter exchanged approximately 43 per cent of its common stock for substantially all of the stock of the old companies which Atlas had acquired under the preceding exchange.* This was likewise a reorganization under *Helvering* v. *Watts, supra.*

In the third step, the new company under the direction of Atlas acquired the assets and business of the old companies in exchange for the entire outstanding common and preferred stock of those companies. This was a reorganization under *Helvering* v. *Minnesota Tea Co.*, 296 U. S. 378.

Viewing these steps, however, in the light of the contracts and the manner in which they were carried out, the conclusion must necessarily follow that the steps were *interdependent* and the completion** of the plan as a whole was the real consideration for each step.

Obviously the exchanges with the stockholders of the old

*The new company also exchanged cash and stock of Atlas, *ante*, pp. 4-6.

**The exchanges were made at one time, on October 7, 1930, at a meeting of representatives of all parties interested (R. 132-136).

companies in the first step could not be completed unless the exchanges in the second step were consummated, because a part of the consideration to be supplied by Atlas in the first step, was shares of stock in the new company which only became available through consummation of the second step. Furthermore, to carry out its obligations to the "stockholders" in the first step, it was necessary for Atlas to cause the consolidation of the old companies into a new corporation, in which, upon completion of the entire transaction, Atlas would be the owner of a majority of all classes of stock, which transaction constitutes the third step.

Before any of these steps could be completed, it was necessary for Atlas, as a part of the plan, to make a sufficient investment (represented by cash and shares of its stock) in the stock of the new company to insure its control and provide it with sufficient assets to carry out its part of the plan.

4. Petitioner assures us (Pet. Br. 20) he is not asking this Court that the separate transfers and exchanges in a " * * * plan of reorganization be viewed as independent transactions with legal consequence different from those which would result were the plan examined at its completion." Proceeding, therefore, on that basis and viewing the transaction at its completion, we find that Atlas had not only acquired a majority of the stock of all classes of the new company (within the express terms of Section 112 (i) (2)) but looking to the substance rather than the form, Atlas had acquired a majority of the stock of all classes and a controlling interest in the business and assets of Peerless and Union in their merged or consolidated form (through ownership of stock of the consolidated company) *as a part of* a single transaction and plan which had no other purpose, from the beginning. As this Court said in *Weiss* v. *Stearn*, 265 U. S. 242: " * * * when applying the provisions of the Sixteenth Amendment and income laws enacted thereunder we must regard matters of substance and not mere form."

From the beginning to the end there were but two parties dealing with each other at arms length, Atlas on the one side and the "stockholders" on the other. These interests thus remained until the completion of the plan when their respective interests converged into the joint enterprise thereafter conducted by the new company. Atlas emerges with a majority of the stock of all classes of the new company, now representing a consolidation of the old companies and the "stockholders" reappear as the owners of a substantial interest in the consolidated enterprise represented by their stockholdings in Atlas and in the new company. The legal significance of the Atlas stock received by the taxpayer, in so far as it bears on the continuity of his interest in the assets transferred, will be considered at length in the second phase of this Argument.

But even if the acquisition by Atlas of a majority of the stock of all classes of the new company is treated as "in connection with" other exchanges and transfers in the plan, rather than as the necessary and ultimate end of the consummation of the plan as a whole (as Respondent contends) it would none the less come within the literal terms of Section 112 (i) (2) since that definition is not limited to any one step in a series of exchanges contemplated under a single plan of reorganization. If the transitory steps heretofore referred to are considered, there are at least two other "acquisitions" which would come within the statutory provision in question since Atlas in one transitory step acquired substantially all of the stock of the old companies and in the consummation of another step, the new company acquired all of the stock of the old companies held by Atlas. These acquisitions were, however, only to accomplish the final purpose and result, *i. e.*, the merging of the business and assets of the old companies into the new and an acquisition by Atlas of a controlling interest therein through acquiring the requisite stock in the new company which qualified it as "a party

to the reorganization'' within the literal terms of Section 112 (i) (2).

The Petitioner admits (Pet. Br. 26) that ''the plan, as carried out, was to have a subsidiary of Atlas, organized for the purpose, acquire the stock and the assets of the competing corporation''. Had Atlas not become the owner of a majority of the stock as a part of the plan, which, when consummated, resulted in the reorganization of the old companies into the new, the latter would not have been its subsidiary.

5. As supporting his contention that Atlas was not ''a party to the reorganization'' within the intendment of Section 112 (i) (2) and 112 (b) (3) of the statute, Petitioner cites *Commissioner* v. *Groman,* 86 Fed. (2d) 670 (C. C. A. 7th) pending in this Court, No. 21, October Term, 1937, and *Bus and Transport Securities Corp.* v. *Helvering,* 296 U. S. 391.

It will be observed that the Commissioner in his brief filed with the Circuit Court of Appeals in *Commissioner* v. *Groman, supra,* (Pet. Br. Below 14), stated, in commenting on the conclusion of the Court in *Fifth Avenue Bank of N. Y., Exr.* v. *Commissioner, supra,* ''that the statutory definition of 'party to a reorganization' is not all inclusive; * * *'', that this construction of the statutory definition is not objectionable but that it had no application there because ''Glidden'' was neither a corporation resulting from a reorganization, nor did it acquire a majority of the stock of another corporation. The Seventh Circuit Court of Appeals, however, apparently based its opinion that ''Glidden'' was not a ''party'' in the statutory sense solely on a narrow construction of Section 112 (i) (2) since it concludes (at page 672) that ''it would, we think, be a forced construction to assume that under such circumstances there were parties other than those defined by the statute''. The Court below, in the instant case, concluded that the Seventh Circuit Court of Appeals had apparently overlooked the interpretative regulations (Article 577, Regulations 74)

which provide that the statute "simply enumerates certain cases with respect to which doubt might arise." (R. 205) It would seem to follow that the decision in the *Groman* case was based solely on the fact that "Glidden" did not acquire a majority of the stock of all classes of the new company to come within the narrow confines of one of the specific examples set forth in Section 112 (i) (2), its dicta notwithstanding.

Respondent, in his brief filed in this Court in opposition to the issuance of a Writ of Certiorari (Resp. Br. 12-14) commented at length on this distinction between the facts in the *Groman* case and those in the instant case, pointing out that Atlas did acquire the requisite majority of stock of all classes of the new company and that the Court below found that Atlas was "a party to a reorganization" within the literal terms of Section 112 (i) (2). The conflict is merely in that part of the decision in the *Groman* case which held that the definition in the above statutory provision was all-inclusive. The real conflict was with *Fifth Avenue Bank of N. Y., Exr.* v. *Commissioner, supra.*

This Court in its opinion in *Bus and Transport Securities Corp.* v. *Helvering, supra,* rejected the contentions of the taxpayer because it found in the transaction no semblance of a merger or reorganization. It follows that if there was no reorganization there could be no "parties" to a reorganization. The transaction there also seems clearly to be outside of the purposes and intent of the reorganization statutes, and as concluded by the Third Circuit Court of Appeals in that case (79 Fed. (2d) 509) clearly within the decision of this Court in *Gregory* v. *Helvering,* 293 U. S. 465.

In *Union Trust Company, Executor,* v. *Heiner,* (W. D., Pa.) 18 Fed. Supp. 801, cited in Petitoner's brief as in conflict with the decision in the instant case, the Court distinguished the facts there from those in the instant case and in *Fifth Avenue Bank of N. Y., Exr.* v. *Commissioner, supra,* in that the taxpayer received no stock in the subsidiary corporation. The facts are not sufficiently set forth in the opin-

ion in the *Union Trust Company* case to determine to what extent, if any, the parent corporation participated as an actual party to the transaction. In that decision also the Court was not called upon to consider what corporations were "parties to a reorganization" because it failed to find that there was a reorganization within the statutory provisions.

The following cases involve facts comparable to those in the instant case and in each one the decision supports the position taken by the Respondent in this section of the Argument that Atlas is "a party to a reorganization" within the literal terms of Section 112 (i) (2). *Ballwood Co.* v. *Commissioner*, 84 Fed. (2d) 733 (C. C. A. 3rd); *Henritze* v. *Commissioner*, 28 B. T. A. 1173; *Armstrong* v. *Commissioner*, 31 B. T. A. 418; *Tulsa Oxygen Company* v. *Commissioner*, 18 B. T. A. 1283; and *First National Bank of Champlain, N. Y.* v. *Commissioner*, 21 B. T. A. 415.

Unlike the facts in the instant case wherein the taxpayer received stock not only of Atlas but also of the new company, it will be noted that in all of the above cited cases the taxpayer received stock *only* in the corporation comparable to Atlas.

In *First National Bank of Champlain, N. Y.* v. *Commissioner, supra*, involving the construction of section 203 (b) (2) of the 1926 Act (identical to section 112 (b)(3) of the 1928 Act) it was the Commissioner who contended that International Paper Company was "a party to a reorganization" because it acquired all of the stock of the new company (Canadian Corporation) which acquired all the assets and liabilities of Riordan Pulp and Paper Company.

The taxpayer there, unlike Respondent in the instant case, however, acquired none of the stock of the new company. The Board considered intervention of the new company to hold title to the former properties of Riordan was immaterial and that even if it were considered that there were two simultaneous transactions, the acquisition of the properties of Riordan by the new company and the ac-

quisition of the new company's stock by the International Paper Company, it would still be a reorganization because both transactions fall within the specific terms of Section 203 (h) (1) (A) of the 1926 Act defining reorganization.

In *Tulsa Oxygen Company* v. *Commissioner, supra,* the transfer by taxpayer of its assets to a subsidiary of "Union Carbide", under an agreement with the latter, (but subsequently changed by a substitution of one of its subsidiaries as the contracting party) for shares of its stock held by still another subsidiary was held to constitute a statutory reorganization in which "Union Carbide" was necessarily considered a party within the statutory sense, since the gain resulting to taxpayer on the receipt of its stock was held non-recognizable under section 203 (b)(3) of the 1924 Act. Like the preceding case cited, taxpayer received no stock in the new company. The Commissioner acquiesced in this decision which was rendered in 1930 (Cum. Bull. IX-2; p. 60). The 1932 Act, passed two years later, carried provisions identical to Section 203 (b)(3) of the 1926 Act and 112 (i)(2) of the 1928 Act.

The decision of the Board in *Independent Oil Company* v. *Commissioner,* 35 B. T. A. —, No. 8, decided November 5, 1936, is very similar in its facts to the instant case. While the principal consideration received by taxpayer was stock of the parent company (Vacuum), it also acquired 8750 out of 35,000 shares of the common stock of the new company. Under the plan, however, the parent company was given a ten-year option to acquire from taxpayer said 8750 shares of the new company.

Vacuum was held to be a party to the reorganization under the definition of Section 112 (i) (2) since it acquired at least a majority of all classes of the new company's stock. To the same effect see *Henritze* v. *Commissioner, supra,* and *Armstrong* v. *Commissioner, supra.*

II.

Atlas was "a party to the reorganization" within the terms of Section 112 (b) (3) because of its indispensable participation in and inseparable connection with the entire transaction.

1. Referring to the various transfers and exchanges constituting the transaction wherein the taxpayer received Atlas stock, it was found by the Board as a fact, which the Court below held conclusive upon it, that:

> "* * * Atlas was the mainspring of the entire proceeding and without its participation there would have been no reorganization and consolidation into the new company." (R. 141)

This finding was based upon the following more specific evidentiary facts established by Respondent before the Board:

1. Atlas executives conceived the plan (R. 129, 155, 175);
2. Atlas had sound business reasons for desiring to obtain control of the business and assets of Peerless and Union (R. 129, 141, 154-155);
3. Atlas initiated negotiations, and through its agents contracted for and was a party in fact to the various exchanges effectuating the reorganization (R. 130-136, 155, 160, 173-177, 182-190);
4. Atlas supplied the principal consideration, to-wit: its own stock and cash (R. 22, 131-132);
5. Atlas caused the new company to be organized and caused its own nominees to be made its President and Vice-President (R. 22, 131);
6. Atlas guaranteed performance of the new company's obligations regarding income tax payments resulting from the consummation of the plan (Exhibits F, G, H, and J,—R. 88-103, 135);
7. Atlas supplied the new company with the needed working capital (R. 22, 132).

Atlas' indispensable participation in and inseparable connection with the transaction being thus established, the issue arises as to whether or not it follows therefrom that Atlas was "a party to the reorganization", within the meaning of that phrase as used in Section 112 (b) (3). This issue constitutes the second main section of Respondent's argument. It will be considered from a point of view entirely independent of the question of whether or not Atlas has qualified as a party to the reorganization here within the literal terms of Section 112 (i)(2), to which question the first main section of the Respondent's argument was devoted.

2. On this issue it should be observed at the outset that Congress, in describing "a party to a reorganization", in Section 112 (i)(2) did not purport to write an all-inclusive definition of the phrase. This subsection, in contrast to Section 112 (i)(1) which defines what "reorganization" *means*, uses, instead, the word *"includes"*. This clearly imports that Congress intended that there are parties not qualifying within the specific examples inserted in the subsection, who nevertheless may be parties to the reorganization within the statutory meaning of that phrase, as used in Section 112 (b)(3).

This connotation of the word "includes" is not left to speculation, but is made explicit by the definition of that word in Section 701 (b) of the 1928 Act, which provides:

> "The terms 'includes' and 'including' when used in a definition contained in this Act shall not be deemed to exclude other things otherwise within the meaning of the term defined."

See in this connection *Helvering* v. *Morgan's, Inc.*, 293 U. S. 121.

Furthermore, in Article 577 of Regulations 74 (promulgated under the Revenue Act of 1928) it is stated, with respect to the definition in Section 112 (i)(2) of "a party to a reorganization":

"This definition is not an all-inclusive one, but simply enumerates certain cases with respect to which doubt might arise."

It is significant that Section 112 (i)(2) of the Revenue Act of 1928 is a re-enactment in identical language of Section 203 (h)(2) of the 1924 and 1926 Acts, and was re-enacted as Section 112 (i)(2) of the 1932 Act. The Regulations promulgated under these various Acts all contain a reference to this definition in language identical with that quoted above. Since this Section has been re-enacted without change in three Revenue Acts subsequent to its original enactment in 1924, and since Regulations under such Acts have been promulgated explaining it in identical language, Congress must be taken, in re-enacting the Section, to have approved such regulations. See *Helvering* v. *Bliss,* 293 U. S. 144; *Helvering* v. *Minnesota Tea Company, supra.*

Petitioner in his brief argues that Section 112 (i)(2) must be read as if it were nothing more nor less than a part of Section 112 (i)(1), from which he concludes that if Atlas was not one of the reorganized parties under Section 112 (i)(1), it could not be a party to a reorganization within the purport of Section 112 (i)(2). But this treatment of the latter section makes it an entirely unnecessary appendage to the reorganization provisions of the Act instead of an actual and explanatory part thereof, as Congress intended. Section 112 (i)(2) is no more to be read as limited by Section 112 (i)(1) than is Section 112 (i)(1)(A) to be given a narrow and restricted significance because of Section 112 (i)(1)(B). *Helvering* v. *Minnesota Tea Co., supra.* To complete the analogy it is to be noted that Section 112 (i)(2) was, as was Section 112 (i)(1)(B), incorporated into the tax laws for the first time in the 1924 Act, while the provisions of Section 112 (i)(1)(A) were contained in the 1921 Act. See also the decision in *John A. Nelson Company* v. *Helvering,* 296 U. S. 374, 377, where, in the Opinion of this Court, Mr. Justice McReynolds pointed out that Section 203 (h) (1) (A) of the 1926 Act "* * * must not be confused

with paragraph (h) (2) * * * ", which corresponds to Section 112 (i)(2) of the 1928 Act.

Respondent's contention in this respect is further substantiated by the fact that Section 112 (i)(2) makes no specific mention of the situation in which one corporation exchanges its property for stock of another corporation. Notwithstanding this fact, in *Helvering* v. *Minnesota Tea Co., supra,* and *John A. Nelson Company* v. *Helvering, supra,* this Court necessarily determined in holding that the transactions there resulted in a statutory reorganization, that the corporation whose property or stock was acquired was "a party to the reorganization" within the plain intendment of Section 112 (b)(4). This represents a judicial determination by this Court that Section 112 (i)(2) does not constitute an "all-inclusive" definition of the phrase "a party to a reorganization".

3. The Respondent contends that Atlas, because of its indispensable participation in and inseparable connection with the reorganization which resulted in the consolidation of Peerless, Union and Black Diamond into a new corporation under Atlas' control, must be *"included"* as a party to that reorganization within the meaning which Congress intended to give to that phrase, in describing it in Section 112 (b) (3).

While this Court may have considered this question in reaching its opinions in *Helvering* v. *Watts, supra,* and the *Minnesota Tea Co.* case, *supra,* such opinions do not specifically discuss this point. It has, however, been specifically discussed in a number of cases before the Board of Tax Appeals and before the Federal Circuit Courts of Appeal. See *Tulsa Oxygen Co.* v. *Commissioner, supra; Independent Oil Company* v. *Commissioner, supra; Fifth Avenue Bank of New York, Exr.* v. *Commissioner, supra.*

In each of the foregoing cases there was a corporation in a position analogous to that of Atlas in the transactions here, which corporation was not itself reorganized. Stock

of said corporation was acquired by the taxpayer in each case, in exchange for a prior direct or indirect interest of the taxpayer in assets transferred under the plan to its subsidiary. In each of the foregoing cases such corporation (comparable to Atlas) was held to be a party to the reorganization, and the gain or loss resulting to taxpayer in the transaction was, therefore, not recognized. It is true that the series of transactions which culminated in the result described above have not been the same in each case. For instance, in the *Ballwood* case it was the taxpayer who undertook the organization of the subsidiary corporation to which its assets were transferred and the stock of that corporation in its hands was then exchanged for stock of the corporation (comparable to Atlas) which was not reorganized. On the other hand, in the *Fifth Avenue Bank* case, the circumstances were very similar on this point to the facts in the instant case. In each of the cases, however, a party intimately connected with the transaction, whether or not a party within the literal terms of Section 112 (i)(2), was held to be a party to the reorganization.

Tending to a contrary conclusion on this general question is the case of *Commissioner* v. *Groman, supra.* Inasmuch as this case has been analyzed in an earlier portion of this brief, it is deemed unnecessary to discuss it further here.

In addition to the *Groman* case, the Petitioner has cited, in opposition to Respondent's contentions in this connection, the cases of *Bus and Transport Securities Corporation* v. *Helvering, supra,* and *Union Trust Company, Exr.,* v. *Heiner, supra.* Respondent takes issue with Petitioners' contention that these cases control the instant case. *Bus and Transport Securities Corporation* v. *Helvering, supra,* has been analyzed at length in Petitioner's brief, but he has failed to state the controlling factor in the decision, as made clear by the opinion of this Court, namely, that in the various transfers and exchanges there involved, there was no

semblance of a merger or consolidation. Similarly, the Court in *Union Trust Company, Exr.*, v. *Heiner, supra,* failed to find a reorganization in the facts before it. Obviously it is futile to discuss whether or not a corporation can be a party to a reorganization if there is no reorganization to begin with. *Claude Neon Lights, Inc.*, v. *Commissioner,* 35 B. T. A. —, No. 63. The Petitioner has conceded in the instant case that there was a reorganization and the sole question is whether or not Atlas was a party to it. In this connection, it should be observed that in the argument of the instant case in the Court below, Petitioner laid great stress upon the *Bus and Transport Securities Corporation* case. The Court, however, held that case to be clearly distinguishable on its facts, and not in any way determinative of the question here involved.

With further reference to the Petitioner's argument, in the footnote on page 24 of his brief, that the Commissioner has consistently refused to consider as parties to the reorganization those corporations which play an active role in its instigation and financing, Petitioner has doubtless overlooked the significant fact that the Commissioner acquiesced in the decision in *Tulsa Oxygen Company* v. *Commissioner, supra* (See Cum. Bull. IX-2, p. 60); and also the fact that in *First National Bank of Champlain, N. Y., supra,* it was the Commissioner himself who sought to establish that the party in the position analogous to that of Atlas here was a party to the reorganization. Furthermore, although by the time the decision of the Circuit Court of Appeals for the Third Circuit in *Fifth Avenue Bank of New York, Exr.*, v. *Commissioner, supra,* had been rendered, it was apparent that a federal question of considerable importance in the administration of the Revenue Laws was involved, the Commissioner did not petition this Court for issuance of a Writ of Certiorari in that case.

4. Apart from questions of statutory construction, and the inseparability of the various steps in the transaction at bar, there remains the question whether it is open for

Petitioner to argue before this Court that Atlas' stock in the taxpayer's hands did not represent a sufficient continuity of interest in the assets transferred to bring it within the exemption provisions of Section 112(b)(3), and the further question, if Petitioner may be heard on this point, whether his argument is sound.

Respondent submits that Petitioner cannot now raise for the first time the question of such lack of continuity of interest, because he did not raise that question either before the Board of Tax Appeals or before the Circuit Court of Appeals. (*Helvering* v. *Minnesota Tea Co., supra; Helvering* v. *Tex-Penn Oil Co.*, 300 U. S. 481) In the Board the issue was primarily whether Atlas acquired a majority of the stock of all classes of the new company and whether the transaction, as a whole, constituted a plan of reorganization. The Board having held against the Commissioner on these points he came to the Court below on the sole issue that Atlas was not an open and signatory party to the basic agreements in pursuance to which the exchanges and transfers were made, but admitted that a statutory reorganization had been effected by the consolidation of the old companies into the new company in which Atlas acquired a majority of the stock of all classes. While in substance Petitioner here persists in the issue that Atlas was not a party to the exchanges, which consummated the reorganization (although admitting that Atlas acquired a majority of the stock of all classes of the new company), he contends that the stock of Atlas does not represent to Respondent a sufficient continuity of interest in the assets and business transferred by Peerless to the new company. No mention whatever is made until the case reaches this Court of the question of "continuity of interest," nor were any cases cited in his Brief below, on that precise point.

Even if it is open to Petitioner to raise the issue of continuity of interest at this late stage in the proceedings, neither the facts nor the law sustain his position. This will be apparent upon an examination of the reason and purpose

of Congress in providing for non-recognition of gain in certain reorganization transactions, and the application of such reasons and purpose to the facts in the instant case.

Before undertaking this examination, it should be observed that the necessity for continuity of interest has not been passed upon by this Court in connection with the specific question whether a corporation, not itself reorganized, can qualify as a "party", in the statutory sense, to an admitted reorganization. In view of the fact that Sec. 112 (i)(2) was enacted to include within the definition of a "party to a reorganization" certain doubtful cases, this Court may conclude that in determining what corporations qualify as parties to an *admitted reorganization,* Congress intended that the definition be given a liberal construction so as not to require the spelling out of a continuity of interest in the transferred assets, as must be done to establish in the first instance that there has been a reorganization. If this Court should so conclude, then further consideration of this question would be unnecessary. Respondent maintains, however, that if it is required of him to demonstrate that his acquisition of Atlas stock represented a continuity of interest in the assets with which he was formerly identified, then that requirement is met in the instant case.

The fundamental reason for non-recognition of gain in exchanges of securities involved in a reorganization is that after the exchanges the taxpayer's money is still invested in the same interests or business as that in which it was originally made, although in a modified corporate form. A tax on the profit is deferred until it is realized in cash, or other property not of the same kind. The underlying principle, therefore, is not tax exemption, but tax postponement.

This Court in construing the parenthetical phrase in Section 112 (i)(1)(A) has interpreted its meaning in such a way as to require that the transferor must retain a continuity of interest of substantially the same character in the assets transferred. In so doing, it has tended to make the test as to whether or not there is continu-

ity of interest determinative of whether the reorganization is one in which gain or loss is to be recognized in the transaction. Obviously, it is the taxpayer's continued interest in or identification with the assets with which he parts, as represented in what he receives, that the Court examines.

This test as to continuity of interest has been recognized and applied by this Court in several cases. In *Pinellas Ice and Cold Storage Company* v. *Commissioner*, 287 U. S. 462, this Court stated that to constitute a transaction within the parenthetical expression of Section 112 (i)(1)(A), "the seller must acquire an interest in the affairs of the purchasing company more definite than that incident to ownership of its short-term purchase-money notes." In later cases, this Court added that "this interest must be definite and material; it must represent a substantial part of the value of the thing transferred" but that the fact "that the relationship of the taxpayer to the assets conveyed was substantially changed" did not take the case out of the statute (*Helvering* v. *Minnesota Tea Company, supra*); and that "the statute does not require participation in the management of the purchaser * * *" (*John A. Nelson Company* v. *Helvering, supra*).

In *Helvering* v. *Watts, supra,* which we submit is a parallel to the present case, the taxpayer with two other individuals, owned all of the common stock of Ferro-Alloys. Pursuant to an agreement with the Vanadium Company, they transferred all of their stock in Ferro-Alloys to Vanadium in exchange for certain bonds of Ferro-Alloys, which were guaranteed by Vanadium, and certain shares of Vanadium common stock, and thereafter Ferro-Alloys continued in business. This Court held that the gain resulting from the acquisition by taxpayer of the Vanadium stock was not taxable.

If we analyze these facts, we find that before the reorganization took place, the taxpayer, an individual, had an interest in the business and assets of Ferro-Alloys, through

ownership of stock in that company. At the conclusion of the transfer and exchange he no longer owned this stock, but in its place had received stock in Vanadium, a corporation which had acquired all of the stock of Ferro-Alloys. In addition, the taxpayer had received certain bonds of Ferro-Alloys, guaranteed by Vanadium. This Court, in finding that the gain resulting from the acquisition of the stock and bonds was non-taxable, determined that there had been a reorganization, and that the Vanadium stock in taxpayer's hands after consummation of the transaction represented a continuity of the taxpayer's former interest in the business and assets of Ferro-Alloys, through Vanadium's ownership of all of Ferro-Alloys stock.

In the instant case, before Atlas came into the picture the taxpayer owned preferred and common stock of Peerless and thus had an interest in its business and affairs. Under the plan of reorganization, he agreed that the business and assets of Peerless should be transferred to another company (the new company) and that he would exchange his Peerless stock for cash, stock of the new company (corresponding to the bonds received by taxpayer in the *Watts* case), and preferred and common stock of the corporation which was to control the new company (corresponding to the Vanadium stock in the *Watts* case). Thus, at the consummation of the plan the taxpayer owned stock of the company which emerges from the reorganization in control of the new company owning the business and assets with which taxpayer had been formerly identified as a stockholder of Peerless. The only difference between this case and the *Watts* case, is that here the form of the ownership of the business and assets in which taxpayer was interested has changed, in that, instead of remaining in their original corporate setting, as in the *Watts* case, they have, as a part of the plan to which taxpayer subscribed, been combined with other business and assets (of Union) into a new and enlarged corporate structure. This difference is insubstantial and entirely immaterial from the viewpoint of the tax-

payer's continuity of interest in the original business and assets of Peerless. In both cases at the conclusion of the reorganization transaction the taxpayer is equally removed from the assets and business with which he was originally identified.

It is respectfully submitted, therefore, that *Helvering* v. *Watts* is squarely in point and is an authoritative precedent in a decision of this Court showing continuity of interest here to establish non-recognition of taxpayer's gain resulting from his acquisition of preferred and common stock of Atlas.

In addition to the discussion of continuity of interest by this Court in the foregoing cases, the Respondent's conclusions on this point are also supported in the opinions in the following cases: *Cortland Specialty Company* v. *Commissioner*, 60 Fed. (2d) 937 (C.C.A. 2nd), certiorari denied, 288 U. S. 599; *Fifth Avenue Bank of N. Y., Exr.* v. *Commissioner, supra; Commissioner* v. *Kitselman*, 89 Fed. (2d) 458 (C. C. A. 7th); *Western Power Corp.* v. *Commissioner*, 34 B. T. A. 618; *Independent Oil Company* v. *Commissioner, supra; Kaspare Cohn Co., Ltd.*, v. *Commissioner*, 35 B. T. A. —, No. 91; *Tyng* v. *Commissioner*, 36 B. T. A.—, No. 4.

5. Apart from the authority of the *Watts* case, it is submitted that, on principle, it is logical to hold that the ownership of stock of a parent company represents a definite interest in the business and assets of a subsidiary. The decisions of this Court hereinabove referred to disclose that the problem is not in what precise *form* the interest is retained but whether or not it is real and substantial. Thus, in *Pinellas Ice and Cold Storage Company* v. *Commissioner, supra,* although the taxpayer had received what are ordinarily termed securities, *i. e.*, short term notes, it was held that continuity of interest was lacking because these securities represented little, if anything, more than cash so far as taxpayer's future identification with the former enterprise was concerned.

In contrast, in *John A. Nelson Co.* v. *Helvering, supra,* preferred stock of the company acquiring the business and assets with which the taxpayer had been identified was held substantially to represent a continuation of that identification within the purview of the reorganization sections of the tax law, even though such preferred stock carried with it no voting power.

From this comparison it would appear that the nature of the security received by the taxpayer must, in some way, import that the taxpayer will *continue* his identification with the business and affairs of that enterprise in a material and substantial way in a manner somewhat akin to his prior identification. From this point of view, it is respectfully submitted that the stock of a corporation which takes over the business and assets with which the taxpayer has been identified, and places them in the hands of another corporation which it controls, represents as substantial a guaranty of a continuation of taxpayer's identification with that business and those assets as if he had received stock of the controlled corporation, or as if the assets themselves had been acquired by the controlling corporation.

Here again *Bus and Transport Securities Corporation* v. *Helvering, supra,* upon which Petitioner appears to place so much reliance, must be distinguished. In that case to be sure, some sort of remote relationship between the taxpayer and the stock of the bus companies with which it parted may be spelled out of the situation resulting from the consummation of the various transfers. But this is to be done only by tracing that relationship through an elaborate super-structure of corporate entities, at least two of which seemed to have been called into being not for any continuing purpose in connection with the operation of the business, either of the bus companies or of Public Service Corporation of New Jersey, but for the sole purpose of acquiring and transferring stock, after which their corporate functions ceased. This Court refused to characterize such a relationship or interest as definite and immediate, and

thus concluded that no true reorganization had taken place. But this is a far cry from refusing to find such definite and immediate interest here, where the new company ultimately acquiring the business and assets with which taxpayer had been identified, was to utilize them in the normal and continuing conduct of its business. Nor can it be a denial of definite and immediate interest in the sense in which those terms were used in *Bus and Transport Securities Corporation* v. *Helvering, supra,* that the taxpayer's interest in his former property takes the form, after consummation of the reorganization, of stock in a company which in a normal and thoroughly unartificial way controls the corporation which has acquired that property.

To summarize the situation in the instant case in another way, the fundamental and dominating idea of the whole transaction from the taxpayer's point of view was that he would retain an active and substantial continuing interest in the same business and affairs with which he was connected prior to the consummation of the plan of reorganization. He was approached by Atlas with a plan which, in its essence, consisted in no more than a change in the form of the business in which he was engaged to the extent that it would be combined with another competing business, and the two so combined would be taken in under the control of a third and larger corporation, to-wit, Atlas. To this he agreed, and the consideration for which he asked and which he received, was that his identification with his original enterprise would be continued, not only through his participating in the new and larger enterprise through his stock ownership in the new company, but also through stock ownership in the company which would manage and control it. How can it reasonably be argued that this latter company, Atlas, was not a party to the transaction in the ordinary and usual meaning of that phrase, or that Congress, in legislating on the subject to provide for non-recognition of gain or loss in certain described cases without expressly denying it in others, could have intended that this simple and normal situation should

be excluded? What phrase would be more apt in describing the relation of Atlas to the reorganization than that it was a "party" thereto?

CONCLUSION.

In view of the foregoing, the decision of the Circuit Court of Appeals should be affirmed.

Respectfully submitted,

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APPENDIX.

Revenue Act of 1928, c. 852, 45 Stat. 791:

Sec. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

(b) *Exchanges solely in kind.*—

* * * * * *

(3) *Stock for stock on reorganization.*—No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

(4) *Same—Gain of corporation.*—No gain or loss shall be recognized if a corporation a party to a reorganization exchanges property, in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization.

* * * * * *

(c) *Gain from exchanges not solely in kind.*—

(1) If an exchange would be within the provisions of subsection (b) (1), (2), (3), or (5) of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph to be received without the recognition of gain, but also of other property or money, then the gain, if any, to the recipient shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property.

(2) If a distribution made in pursuance of a plan of reorganization is within the provisions of paragraph (1) of this subsection but has the effect of the distribution of a taxable dividend, then there shall be taxed as a dividend to each distributee such an amount of the gain recognized under paragraph (1) as is not in excess of

his ratable share of the undistributed earnings and profits of the corporation accumulated after February 28, 1913. The remainder, if any, of the gain recognized under paragraph (1) shall be taxed as a gain from the exchange of property.

(d) *Same—gain of corporation.*—If an exchange would be within the provisions of subsection (b) (4) of this section if it were not for the fact that the property received in exchange consists not only of stock or securities permitted by such paragraph to be received without the recognition of gain, but also of other property or money, then—

(1) If the corporation receiving such other property or money distributes it in pursuance of the plan of reorganization, no gain to the corporation shall be recognized from the exchange, but

(2) If the corporation receiving such other property or money does not distribute it in pursuance of the plan of reorganization, the gain, if any, to the corporation shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property so received, which is not so distributed.

* * * * * * *

(i) *Definition of reorganization.*—As used in this section and sections 113 and 115—

(1) The term "reorganization" means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation), or (B) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (C) a recapitalization, or (D) a mere change in identity, form, or place of organization, however effected.

(2) The term "a party to a reorganization" includes a corporation resulting from a reorganization and includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation.

(j) *Definition of control.*—As used in this section, the term "control" means the ownership of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of the corporation.

Treasury Regulations 74, promulgated under the Revenue Act of 1928:

Art. 577. *Definitions.*—The term "reorganization", as used in sections 112, 113, and 115 means—

(1) A merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation),

(2) A transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred,

(3) A recapitalization, or

(4) A mere change in identity, form, or place of organization, however effected.

The term "a party to a reorganization" as used in sections 112 and 113 includes a corporation resulting from a reorganization and includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation. This definition is not an all-inclusive one, but simply enumerates certain cases with respect to which doubt might arise.

A person is, or two or more persons are, "in control" of a corporation, within the meaning of section 112, when owning—

(1) At least 80 per cent of the voting stock, and

(2) At least 80 per cent of the total number of shares of all other classes of stock of the corporation.

As used in section 112, as well as in other provisions of the Act, the conjunction "or" is used to denote both the conjunctive and the disjunctive, and the singular is used to include the plural. For example, the provisions of article 574 are complied with if "stock and securities" are received in exchange as well as if "stock or securities" are received, and if securities in the same corporation, together with securities in another corporation a party to the reorganization or in other corporations parties to the reorganization, are received in exchange.